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May 18, 2007

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VIA E-FILEING AND HAND DELIVERY

Charles L.A. Terreni, Esquire
Chief Clerk/Administrator
Public Service Commission of South Carolina
101 Executive Center Dr., Suite 100
Columbia, SC 29210

Re: Application of Lockhart Power Company for a Rate Increase
Docket No. 2007-33-E

Dear Mr. Terreni:

Enclosed please find the original and one copy of the Settlement Agreement along with the Settlement Testimony and Exhibits of Malini Gandhi and A. Randy Watts in the above referenced docket. The Settlement Testimony and Exhibits of Malini Gandhi and A. Randy Watts are included with the Settlement Agreement as Exhibits B and C, respectively. Settlement Exhibit A is the Settlement Testimony and Exhibits of Paul R. Moul and will be filed early next week.

Please note that the attached documents are exact duplicates, with the exception of the form of the signature, of the e-filed copy submitted to the Commission in accordance with its electronic filing instructions.

By copy of this letter we are also serving all other parties of record. Do not hesitate to let me know if you have any questions.

Sincerely,

Shannon Bowyer Hudson

SBH/pjm

cc: M. John Bowen, Jr., Esquire
Scott Elliott, Esquire

BEFORE
THE PUBLIC SERVICE COMMISSION OF
SOUTH CAROLINA
DOCKET NO. 2007-33-E

IN RE:

Application of Lockhart Power Company)	CERTIFICATE OF SERVICE
for a Rate Increase)	

This is to certify that I, Susan Hauptmann, an employee with the Office of Regulatory Staff, have this date served one (1) copy each of the **SETTLEMENT AGREEMENT, SETTLEMENT TESTIMONY AND EXHIBITS OF MALINI GANDHI AND SETTLEMENT TESTIMONY AND EXHIBITS OF A. RANDY WATTS** in the above-referenced matter to the person(s) named below by causing said copy to be deposited in the United States Postal Service, first class postage prepaid and affixed thereto, and addressed as shown below:

M. John Bowen, Jr., Esquire
McNair Law Firm, P.A.
Post Office Box 11390
Columbia, SC 29211

Scott Elliott, Esquire
Elliott & Elliott, P.A.
721 Olive Street
Columbia, SC, 29205


Susan Hauptmann

May 18, 2007
Columbia, South Carolina

BEFORE
THE PUBLIC SERVICE COMMISSION OF
SOUTH CAROLINA
DOCKET NO. 2007-33-E

May 18, 2007

Application of Lockhart Power)	
Company for General Increase)	SETTLEMENT AGREEMENT
In Electric Rates)	
_____)	

This Settlement Agreement is made by and between the South Carolina Office of Regulatory Staff (“ORS”), Lockhart Power Company (“Lockhart” or “the Company”), and the South Carolina Energy User’s Committee (“SCEUC”), (together referred to as the “Parties” or sometimes individually as “Party”).

WHEREAS, the Company has prepared and filed an Application seeking an adjustment of its rates and charges set out in its rate schedules for the provision of its electric service;

WHEREAS, the above-captioned proceeding has been established by the Public Service Commission of South Carolina (“Commission”) pursuant to the procedure established in S.C. Code Ann. § 58-27-810 *et. seq.* (Supp. 2006) and the Parties are the only parties of record in this docket;

WHEREAS, ORS has audited the books and records of the Company relative to the matters raised in the Application;

WHEREAS, the Parties have varying legal positions regarding the issues in this case;

WHEREAS, the Parties have engaged in discussions to determine if a settlement of the issues would be in their best interests and in the case of ORS, in the public interest;

WHEREAS, following those discussions the Company and SCEUC have determined that their interests and ORS has determined that the public interest would be best served by stipulating to a comprehensive settlement of all issues pending in the above-captioned case under the terms and conditions set forth herein;

NOW, THEREFORE, the Parties hereby stipulate and agree to the following terms, which, if adopted by the Commission in its Order on the merits of this proceeding, will result in rates which are adequate, just, reasonable, nondiscriminatory, and supported by the evidence of record of this proceeding, and which will allow the Company the opportunity to earn a reasonable rate of return.

1. The Parties agree that no documentary evidence will be offered in the proceeding by the Parties other than: (1) the Application filed by the Company, (2) the exhibits to the testimony referenced in paragraph 2 below, and (3) this Settlement Agreement with Exhibits "A"- "C" attached hereto.

2. The Parties stipulate and agree to include in the hearing record of this case the pre-filed direct testimonies of Bryan D. Stone, Charles R. Parmelee, and Paul W. Inman including all exhibits attached to said pre-filed testimonies, without objection, change or amendment. The Parties also stipulate and agree to include in the hearing record of this case the pre-filed settlement testimonies of Paul R. Moul, Malini Gandhi, and A. Randy Watts, including all exhibits attached to said pre-filed settlement testimonies, without objection, change, or amendment attached hereto and incorporated herein by this reference as Exhibits "A" through

“C”, respectively. Bryan D. Stone, Paul R. Moul, Malini Gandhi, and A. Randy Watts will be presented before the Commission for questions from the Commission. Charles R. Parmelee and Paul W. Inman will also be available for questions from the Commission.

3. The Parties stipulate and agree that the accounting exhibits prepared by ORS and attached as reflected in Exhibits MG-1 through MG-5 of Exhibit “B” attached hereto are fair and reasonable and set forth the Company’s operating expenses, pro forma adjustments, depreciation rates, rate base, return on equity at an agreed upon rate of 12.00%, revenue requirement, and rate of return on rate base.

4. The Parties stipulate and agree that the three rate schedules shown in ARW-2 through ARW-4 of Exhibit “C” attached hereto as well as the Company proposed Schedules C3, GA, OL, SL, EF, O and PM as filed in the Application, including the rates and charges and terms and conditions of service, are fair, just, and reasonable. The Parties further stipulate and agree that the rates contained in said rate schedules are reasonably designed to allow the Company to provide service to its electric customers at rates that are fair, just and reasonable and the opportunity to recover the revenue required to earn a fair return on its investment.

5. ORS is charged by law with the duty to represent the public interest of South Carolina pursuant to S.C. Code § 58-4-10(B) (added by Act 175). S.C. Code § 58-4-10(B)(1) through (3) reads in part as follows:

... ‘public interest’ means a balancing of the following:

- (1) concerns of the using and consuming public with respect to public utility services, regardless of the class of customer;
- (2) economic development and job attraction and retention in South Carolina; and
- (3) preservation of the financial integrity of the State’s public utilities and continued investment in and maintenance of

utility facilities so as to provide reliable and high quality utility services.

ORS believes the agreement reached between the Parties serves the public interest as defined above. The terms of this Settlement Agreement balance the concerns of the using and consuming public while preserving the financial integrity of the Company. ORS also believes the Settlement Agreement promotes economic development within the State of South Carolina. The Parties stipulate and agree to these findings.

6. In its Application, the Company has requested a net increase in annual revenues of \$592,722. As a compromise to their respective positions, the Parties stipulate and agree to a net increase in annual revenues of \$484,291, said increase to be based upon the adjustments reflected in Settlement Exhibits MG-1 through MG-5 shown in Exhibit "B" attached hereto and the return on equity stipulated to by the Parties in Paragraph 7 below.

7. The Parties recognize the value of resolving this proceeding by settlement rather than by litigation and, therefore stipulate and agree for purposes of settlement in this case that a return on equity of 12.00% is just and reasonable under the specific circumstances of this case in the context of a comprehensive settlement of all issues.

8. The Parties further stipulate and agree that the stipulated testimony of record, the Application, and this Settlement Agreement conclusively demonstrate the following: (i) the proposed accounting and pro forma adjustments and depreciation rates reflected in Settlement Exhibits MG-1 through MG-5 shown in Exhibit "B" attached hereto are fair and reasonable and should be adopted by the Commission for ratemaking and reporting purposes; (ii) a return on common equity of 12.00% and a net annual increase in revenues of approximately \$484,291, is fair, just, and reasonable when considered as a part of this stipulation and settlement agreement

in its entirety; (iii) Lockhart's services are being provided in accordance with the requirements set out in the Commission's rules and regulations pertaining to the provisions of electric service, and (iv) Lockhart's rates as proposed in this Settlement Agreement are designed to equitably and reasonably recover the revenue requirement and are just and reasonable and should be adopted by the Commission for service rendered on or after the date of the Order issued by the Commission in this matter. The Parties agree that when the new rates take effect there will be a one month over or under recovery of purchased power costs under the old rates that will be trued-up in the following month.

9. The Parties further agree and stipulate that the three rate schedules shown in ARW-2 through ARW-4 of Exhibit "C" attached hereto as well as the Company proposed Schedules C3, GA, OL, SL, EF, O and PM as filed in the Application, including the rates and charges set forth therein, are fair, just and reasonable, reasonably designed, and should be approved and adopted by the Commission.

10. The Parties request that the purchase of the Pacolet hydroelectric plant and the associated requested rate treatment be approved by the Commission.

11. The Parties agree to advocate that the Commission accept and approve this Settlement Agreement in its entirety as a fair, reasonable and full resolution of the above-captioned proceeding and to take no action inconsistent with its adoption by the Commission. The Parties further agree to cooperate in good faith with one another in recommending to the Commission that this Settlement Agreement be accepted and approved by the Commission. The Parties agree to use reasonable efforts to defend and support any Commission order issued approving this Settlement Agreement and the terms and conditions contained herein.

12. The Parties agree that signing this Settlement Agreement will not constrain, inhibit, impair, or prejudice their arguments made or positions held in other proceedings. If the Commission should decline to approve this Settlement Agreement in its entirety, then any Party desiring to do so may withdraw from the Settlement Agreement without penalty or obligation.

13. This Settlement Agreement shall be interpreted according to South Carolina law.

14. The above terms and conditions fully represent the agreement of the Parties hereto. Therefore, each Party acknowledges its consent and agreement to this Settlement Agreement by affixing its signature or by authorizing its counsel to affix his or her signature to this document where indicated below. Counsel's signature represents his or her representation that his or her client has authorized the execution of the agreement. Facsimile signatures and e-mail signatures shall be as effective as original signatures to bind any party. This document may be signed in counterparts, with the various signature pages combined with the body of the document constituting an original and provable copy of this Settlement Agreement. The Parties agree that in the event any Party should fail to indicate its consent to this Settlement Agreement and the terms contained herein, then this Settlement Agreement shall be null and void and will not be binding on any Party.

WE AGREE:

Representing the South Carolina Office of Regulatory Staff

Shannon Bowyer Hudson
Shannon Bowyer Hudson, Esquire

South Carolina Office of Regulatory Staff

Post Office Box 11263

1441 Main Street (Suite 300)

Columbia, SC 29211

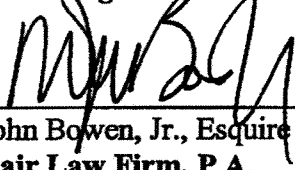
Phone: (803) 737-0889

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E-mail: shudson@regstaff.sc.gov

WE AGREE:

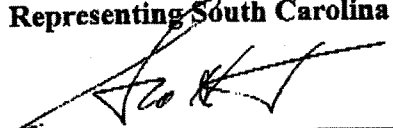
Representing Lockhart Power Company



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WE AGREE:

Representing ³South Carolina Energy Users Committee



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**THE OFFICE OF REGULATORY STAFF
SETTLEMENT TESTIMONY AND
EXHIBITS
OF
MALINI GANDHI, CPA**



**MAY 18, 2007
DOCKET NO. 2007-33-E**

**APPLICATION OF LOCKHART POWER
COMPANY, FOR GENERAL INCREASE IN
ELECTRIC RATES**

SETTLEMENT TESTIMONY OF MALINI GANDHI

FOR

THE OFFICE OF REGULATORY STAFF

DOCKET NO. 2007-33-E

IN RE: LOCKHART POWER COMPANY

Q. MS. GANDHI, WOULD YOU PLEASE STATE YOUR NAME, BUSINESS ADDRESS, AND OCCUPATION?

A. My name is Malini Gandhi. My business addresses is 1441 Main Street, Suite 300, Columbia, South Carolina 29201. I have been employed as Deputy Director of Auditing for the South Carolina Office of Regulatory Staff ("ORS") since June 2006.

Q. WOULD YOU PLEASE STATE YOUR EDUCATIONAL BACKGROUND AND YOUR BUSINESS EXPERIENCE?

A. I received a Bachelors Degree in Business Administration, with a major in Business Finance from the University of Central Oklahoma. I also received a Bachelors Degree with a major in Accounting from the University of Bombay. I am a Certified Public Accountant licensed by the Oklahoma Accountancy Board, with over twenty years of experience in both public and private accounting. In 1993, I was employed by the Public Utility Division of the Oklahoma Corporation Commission and have participated in utility cases involving electric, gas, telephone, and water utility companies. I also managed the Oklahoma Universal Service Fund from 1998 to 2006.

1 **Q. WHAT IS THE PURPOSE OF YOUR SETTLEMENT TESTIMONY**
2 **INVOLVING LOCKHART POWER COMPANY?**

3 A. The purpose of my settlement testimony is to set forth the adjustments agreed upon
4 in the Settlement Agreement ("the Settlement") between ORS, Lockhart Power
5 Company ("Company", "Lockhart" or "Applicant"), and the South Carolina Energy
6 User's Committee ("SCEUC"), collectively referred to as "parties" filed in this
7 docket No. 2007-33-E. These findings and recommendations are shown in detail in
8 the audit report, with attached exhibits.

9 **Q. PLEASE IDENTIFY THE SETTLEMENT EXHIBITS ATTACHED TO**
10 **YOUR PREFILED TESTIMONY.**

11 A. I have attached the Report of the Audit Department ("Audit Report") related to
12 Lockhart Power Company, Docket No. 2007-33-E, Application for General Increase
13 in Electric Rates. The contents of the Audit Report were prepared by me or under
14 my direction and supervision in compliance with recognized accounting and
15 regulatory procedures for electric utility rate cases.

16 **Q. PLEASE EXPLAIN THE CONTENTS OF THE AUDIT REPORT?**

17 A. As outlined in the Index of the Audit Report, the first 4 pages contain the report
18 analysis. The remaining pages consist of settlement exhibits that were prepared to
19 show various aspects of the Company's operations and financial position. The
20 majority of my testimony will refer to Settlement Audit Exhibit MG-1 entitled
21 Operating Experience, Rate Base and Rate of Return. These exhibits were prepared
22 in compliance with the ORS'S standard procedures for electric utility rate
23 applications.

1 Q. WOULD YOU EXPLAIN THE FORMAT OF SETTLEMENT AUDIT
2 EXHIBIT MG-1?

3 A. Yes. Shown in this exhibit are Lockhart's operating experience, rate base, and rate
4 of return for the test year ended December 31, 2005. The exhibit's format is
5 designed to reflect Per Books figures and Proposed Accounting & Pro forma
6 Adjustments per the Settlement necessary to normalize the results of Lockhart's
7 test year operations.

8 Column (1) shows the Total Electric Operations, Per Company Books, for the test
9 year ended December 31, 2005.

10 Column (2) shows proposed accounting and pro forma adjustments, per settlement,
11 designed to normalize Total Electric Operations presented in column (1).

12 Column (3) shows the Company's Total Electric Operations after accounting and pro
13 forma adjustments, per settlement, by adding columns (1) and (2).

14 Column (4) shows the Company's allocation of the Total Electric Operations, Per
15 Books, to the Company's Retail Electric Operations.

16 Column (5) shows the allocation of proposed accounting and pro forma adjustments,
17 per settlement, from Total Electric to Retail Operations.

18 Column (6) shows the Company's Retail Operations after accounting and pro forma
19 adjustments, per settlement, by adding columns (4) and (5).

20 Column (7) shows the calculation of the impact on Retail operating revenues and
21 expenses of the Proposed Increase per the Settlement.

22 Column (8) presents the calculation of the impact on Retail Operations of the
23 settlement increase proposed by the parties by adding columns (6) and (7).

1 **Q. WOULD YOU PLEASE ELABORATE ON THE CALCULATIONS IN**
2 **SETTLEMENT AUDIT EXHIBIT MG-1?**

3 **A.** Yes. All the book balances were verified to detailed accounting records of the
4 Company during the ORS examination.

5 As per Column (1), using Total Electric Operations per company's books for the test
6 year ended December 2005, the total income for return of \$1,849,868, and total rate
7 base of \$16,383,954, the computed rate of return was 11.29%. ORS and Lockhart
8 proposed accounting and pro forma adjustments to normalize the operating
9 experience in column (2) calculated as the Total Electric amounts. Column (3),
10 presents after accounting and pro forma adjustments, per settlement, for Total
11 Electric Operations amounts.

12 The Company's column (4) presents the allocation of the Total Electric booked
13 amount to their Retail Operations. Using Retail Operations, per the Company's
14 filing, total income for return of \$1,373,464, and total rate base of \$12,830,175, the
15 computed rate of return was 10.70%. The proposed accounting and pro forma
16 adjustments, per settlement, were allocated to the Company's Retail Operations in
17 column (5). Column (6), presents Retail Operation amounts after accounting and pro
18 forma adjustments, per settlement, which calculated the total income for return of
19 \$1,151,336, total rate base of \$14,387,296, and a resulting rate of return of 8.00%.

20 The Retail Operations proposed increase per the settlement of \$919,201 is presented
21 in column (7), along with the related adjustments for taxes and customer growth.

22 Lastly, column (8), presents the after proposed increase per the settlement, which

1 calculates the total income for return of \$1,726,973, rate base of \$14,387,296, and a
2 resulting rate of return of 12.00%.

3 **Q. WOULD YOU PLEASE EXPLAIN THE ADJUSTMENTS IN SETTLEMENT**
4 **AUDIT EXHIBIT MG – 2?**

5 A. Yes, the explanations of Accounting and Pro forma Adjustments are listed as
6 ‘Lockhart Total System’, ‘Settlement Total System’ and ‘Settlement Retail
7 Operation’ separately, as follows:

8 **Revenue and Purchased Power Cost Adjustments:**

9 Adjustment(1) – The parties agreed on the proposed Total System rate revenue
10 adjustment to decrease purchased power cost resulting from the acquisition of the
11 Pacolet facility and the purchase of new diesel peaking generation. Details of this
12 adjustment are discussed by the ORS Electric Department Witness, Mr. Randy
13 Watts.

14 Adjustment (2) - Per settlement, ORS and Lockhart agreed on the proposed
15 adjustment for purchased power cost to reflect the reduction in demand payments to
16 the Pacolet Qualified Facility resulting from the Pacolet acquisition and addition of
17 new diesel peaking generation. Details of this adjustment are discussed by the ORS
18 Electric Department Witness, Mr. Randy Watts.

19 **Other Operating Expense Adjustments:**

20 Adjustment (3) – The parties have proposed an increase to Total System production
21 expense of \$210,773 to reflect the additional costs of operating newly acquired
22 generation facilities, and the payroll increase. The resulting impact on Retail
23 production expense is an increase of \$125,895. The components are as follows:

- 1 • 3-A This adjustment increased the production expenses as a result of the
2 Pacolet Hydro Plant acquisition. Details of this adjustment are discussed by
3 the ORS Electric Department Witness, Mr. Randy Watts.
- 4 • 3-B This adjustment increased the production expenses as a result of the
5 purchase of diesel peaking generation. Details of this adjustment are
6 discussed by the ORS Electric Department Witness, Mr. Randy Watts.
- 7 • 3-C This adjustment reflects the allocation, to Total System and Retail
8 Operations production expense, of the wage increase of \$28,785, as explained
9 in Adjustment (4), below.

10 Adjustment (4) – The parties agreed to annualize payroll for hourly, administrative
11 and management salaries based on the last pay period in December 2006. In order to
12 reflect the 2006 annualization adjustment made to the 2005 payroll, a 2 year average
13 was utilized to calculate the expense and capitalization ratio. Further, ORS and
14 Lockhart expensed the portion of the total increased amount by using the expense
15 factor of 75.42% for hourly and 92.16% for administrative and management salaries.
16 The capitalized portion of the ratio is discussed in the adjustment 13-C and was
17 allocated to the Company's Construction Work In Progress ("CWIP"). The
18 settlement proposed increase for the expense portion was allocated to Production,
19 Transmission, Distribution, Administrative & General and Customer Accounting
20 expenses. The expense portion of the adjustment was calculated on a Total System
21 basis and allocated to Retail Operations as follows:

22 (4a) The Total System increase allocated to Transmission expense was \$4,851, of
23 which \$2,862 was allocated to Retail Operations.

1 (4b) The Total System allocated to Distribution expense was \$13,904, of which
2 \$13,696 was allocated to Retail Operations.

3 (4c) The Total System allocated to Customer Accounting expense was \$8,618, of
4 which \$8,343 was allocated to Retail Operations.

5 Adjustment 5 –The parties agreed to increase Administrative and General Expenses
6 for the Total System by \$40,085. The amount allocated to Retail Operations was
7 \$32,917. The components of the adjustments are as follows:

- 8 • 5-A calculated the expense portion of the payroll adjustment allocated to
9 Administrative & General Expenses for hourly and salaried employees. The
10 Total System increase for the expenses by the settlement was \$18,897.
- 11 • 5-B calculated the management transition expense amortization adjustment.
12 Lockhart incurred various expenses related to hiring a new Business Manager
13 in April 2006, to replace the retired Business Manager. The management
14 transition expenses included interviewing, consulting, moving and relocation
15 expenses totaling \$88,056, amortized over 3 years in accordance with the
16 settlement agreement. The Total System amortized amount was \$28,685.
- 17 • 5-C calculated the amortization of the legal cost incurred by Lockhart in the
18 acquisition of Pacolet Hydro Plant. ORS reviewed the actual legal cost of
19 \$31,185 and amortized it over 3 years in accordance with the Settlement
20 agreement. The Total System amortized amount was \$10,395.
- 21 • 5-D calculated the fringe benefits portion of the increased payroll adjustment.
22 The parties removed vacation pay from the calculation of the fringe benefits
23 ratio included in the application. As per settlement, the parties annualized the

1 payroll for 2,080 hours including any vacation or holidays which was
2 consistent with the last Lockhart rate case adjustment. Per settlement, the
3 parties agree on Total System fringe benefits for the amount of \$2,131.

- 4 • 5-E calculated the Settlement adjustment associated with the expenses such as
5 advertising, civic club dues, service awards, one-half of chamber of
6 commerce dues, and other items not considered being necessary for
7 ratemaking purposes. The Total System amount recommended by the parties
8 reduced the Administrative & General Expenses by (\$20,023).

9 Adjustment 6 – This adjustment calculates the amortization of rate case expenses
10 over 3 years, in accordance with the Settlement agreement. Based on the known and
11 measurable rate case expenses of \$70,450, the parties propose to include \$23,483 in
12 the cost of service. This results in a net adjustment of \$6,978 to the Total System and
13 Retail Operations.

14 Adjustment 7 - Depreciation expense was calculated based on the pro forma adjusted
15 plant in service balance as of September 30, 2006 using depreciation rates agreed
16 upon by the parties. The parties propose Total System depreciation expense of
17 \$137,404, and the amount allocated to Retail Operations of \$93,858.

18 Adjustment 8 – The parties propose an increase in Total System expense for Other
19 Taxes, including property taxes, payroll taxes and revenue taxes, of \$81,849. The
20 amount allocated to Retail Operations was \$59,510.

- 21 • 8-A calculated the annualized property taxes for the updated plant balances
22 included in the rate base. The Total System property taxes agreed upon by
23 the parties were \$79,190.

- 8-B calculated payroll taxes associated with the wage adjustment proposed by the parties. The Total System payroll taxes calculated, per settlement, were \$5,126.

- 8-C calculated the adjustment for revenue taxes based on the proposed reduction in revenues. The parties proposed a reduction in Total System expenses of (\$2,467), as a result of revenue reductions.

Adjustment 9 – The parties propose to calculate State Income Taxes at the rate of 5% of taxable income. The reduction for State Income Taxes for the Retail Operations, per settlement, was (\$16,826).

Adjustment 10 – The parties propose to calculate Federal Income Taxes at the rate of 34% of taxable income. The reduction for Federal Income Taxes, at the Retail Operation level, calculated by the parties, was (\$108,697).

Adjustment 11 – This adjustment calculated the Customer Growth for changes in Net Operating Income, per settlement, of (\$485) for Retail Operations based on the factor of .00219 in the application.

Adjustment 14 – The following adjustments resulted from the cost of service study allocations to Total Electric and Retail Operations in accordance with the Settlement agreement:

- (14a) The amortization of FERC Licenses Expense of \$3 allocated to Retail Operations.
- (14b) The Amortization of Investment Tax Credits of \$126 allocated to Retail Operations.

1 **Rate Base Adjustments:**

2 Adjustment 12 – The following adjustments were made to Plant in Service for the
3 Total System amount of \$3,086,301 by agreement of the parties. The amount
4 allocated to Retail Operations, per the Settlement, was \$2,066,568.

- 5 • 12-A calculated the adjustment for the Pacolet Hydro Plant acquisition to be
6 included in the rate base in the amount of \$350,000. Details of this
7 adjustment are discussed by Electric Department witness Mr. Randy Watts.
- 8 • 12-B calculated the adjustment for the diesel peaking plant to be included in
9 the rate base for \$1,767,632. The parties agreed to adjust for the actual
10 known and measurable amount booked by Lockhart in 2006.
- 11 • 12-C adjusts for other known and measurable additions to plant as of
12 September 30, 2006, agreed to by the parties, in the amount of \$968,669.

13 Adjustment 13 – The parties propose to adjust CWIP, on a Total System basis, by
14 (\$983). The amount allocated to retail operations, per Settlement, was \$101,992.

15 Components of the adjustment are as follows:

- 16 • 13-A reflects known and measurable additions to CWIP totaling to
17 \$105,446, on a Total System basis, as of September 30, 2006, as agreed by
18 the parties.
- 19 • 13-B reflects the transfer of completed projects totaling (\$124,297), on a
20 Total System basis, associated with the diesel peaking generation, from
21 CWIP to the plant in service, as agreed by the parties.
- 22 • 13-C calculates the capitalized portion of the payroll adjustment to be
23 included in the rate base. The parties agree to capitalize hourly wages at

24.58% and administrative and management salaries at 7.84% based on the average of Lockhart's expense/capitalization ratio for 2005 and 2006. The same capitalization ratios were applied to the fringe benefits and payroll taxes. This resulted in a Total System adjustment amount of \$17,868 to be included in CWIP.

Adjustment 14 – The following adjustment resulted from the cost of service study allocations to Total Electric and Retail Operations in accordance with the Settlement agreement:

- (14c) The Accumulated Deferred Income Taxes allocated to retail rate base were for (\$27,663).

Adjustment 15 – This adjustment calculates the accumulated depreciation for the known and measurable plant balance as of September 30, 2006, for the Total System amount of \$788,539, as agreed upon by the parties. The allocated amount for Retail Operations, was \$636,210.

Adjustment 16 – The parties propose this adjustment to normalize the Materials and Supplies account balance by calculating a 13 month average from September 2005 through September 2006. The parties agreed upon the 13 month average as a better means to normalize the Materials and Supplies balance. This calculation is consistent with other rate base items updated through September 2006. The Total System amount of the settlement adjustment was (\$4,109) and the amount allocated to Retail Operations was (\$2,892).

Settlement Proposed Increase

Adjustments 17 thru 21 – These adjustments account for the effect of the proposed

1 increase, per settlement, in the exhibit, as follows:

- 2 • (17) Rate Revenue increase proposed by the parties - \$919,201
- 3 • (18) Taxes Other Than Income - \$3,125
- 4 • (19) State Income Taxes - \$45,804
- 5 • (20) Federal Income Taxes - \$295,893
- 6 • (21) Customer Growth - \$1,258

7 **Q. WOULD YOU PLEASE ELABORATE ON THE REMAINING**
8 **SETTLEMENT AUDIT EXHIBITS?**

9 A. Yes. MG-3 shows the computation of Depreciation and Accumulated Depreciation,
10 Exhibit MG-4 shows the computations of Income Taxes, and MG-5 shows the
11 computation of Customer Growth.

12 **Q. WHAT IS THE RATE OF RETURN BEING CALCULATED IN THIS CASE?**

13 A. Settlement Audit Exhibit MG-1 calculated the following rate of return calculations
14 based on total income for return divided by the total rate base in each column listed
15 below:

16 Column (1) Total Electric, per Lockhart's books, the Rate of Return calculated to be
17 11.29%.

18 Column (3) Retail Operations, per Lockhart's books, the Rate of Return calculated to
19 be 10.70%.

20 Column (5) Retail Operations, per settlement after Accounting & Pro forma
21 Adjustments, the Rate of Return calculated to be 8.00%.

22 Column (7) Retail Operations, after Settlement Proposed Increase, calculated a Rate
23 of Return of 12.00%.

1 Q. PLEASE LIST THE AREAS DISCUSSED BY THE ORS ELECTRIC
2 DEPARTMENT WITNESS MR. RANDY WATTS IN HIS SETTLEMENT
3 TESTIMONY.

4 A. Mr. Randy Watts, in the settlement testimony addressed the following areas:

- 5 • Cost of Service allocations
- 6 • Operating Revenues and Purchased Power
- 7 • Acquisition of Pacolet Hydro Plant and the diesel peaking plant addition
- 8 • Depreciation rates
- 9 • Customer Growth

10 Q. DOES THIS CONCLUDE YOUR TESTIMONY?

11 A. Yes, it does.

**REPORT OF THE AUDIT DEPARTMENT
THE OFFICE OF REGULATORY STAFF**

DOCKET NO. 2007-33-E

LOCKHART POWER COMPANY

REPORT OF THE AUDIT DEPARTMENT

THE OFFICE OF REGULATORY STAFF

DOCKET NO. 2007-33-E

LOCKHART POWER COMPANY

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REPORT OF THE AUDIT DEPARTMENT

THE OFFICE OF REGULATORY STAFF

DOCKET NO. 2007-33-E

LOCKHART POWER COMPANY

SYNOPSIS

Total Operating Revenues

	<u>Per Settlement</u>	<u>Per Application</u>
Proposed Increase	\$ 919,201	\$ 1,027,632
After Proposed Increase	\$13,869,213	\$13,977,644
Rate of Return-After Proposed Increase	12.00%	12.50%

Rate of Return on Rate Base

Total Electric

Per Books	11.29%
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Retail Electric

Per Books	10.70%
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After Accounting and Pro Forma Adjustments Per Settlement	8.00%
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After Proposed Increase Per Settlement	12.00%
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REPORT OF THE AUDIT DEPARTMENT
THE OFFICE OF REGULATORY STAFF
DOCKET NO. 2007-33-E
LOCKHART POWER COMPANY

ANALYSIS

The South Carolina Office of Regulatory Staff (“ORS”) Audit Department conducted an examination of the books and records of Lockhart Power Company (“Lockhart” or “the Company”) relative to its application to adjust and increase its retail electric rates as shown in Docket No. 2007-33-E. The examination period covered operating results for the test year ending December 31, 2005, and any applicable known and measurable changes to the test year.

Lockhart Power Company is a wholly-owned subsidiary of Milliken & Company, Inc. Lockhart is a corporation organized in the State of South Carolina on February 12, 1912 by Special Act of the Legislature of South Carolina. The Company’s principal place of business is located in Lockhart, South Carolina. The Company furnishes generation, transmission, distribution and sale of electricity to its customers in five counties: Union, Spartanburg, Cherokee, Chester and York. Lockhart serves approximately 6,400 customers. Lockhart is a small electric company serving a limited geographic area and had no customer complaints during the test year.

ORS respectfully submits the results of its examination as follows:

1. Lockhart filed an application on February 5, 2007 for approval of a general increase in retail electric rates for services provided to its customers.
2. In this application, Lockhart requested a revenue increase of \$1,027,632 for its Retail Operations, which equated to a Rate of Return of 12.50% (Per Company) on

Rate Base after the requested increase.

3. Lockhart's current rates were established by the South Carolina Public Service Commission in the Company's last rate case, Docket No. 2002-122-E, Order No. 2002-794, dated November 22, 2002.

The following exhibits are related to Lockhart's application for a proposed increase:

SETTLEMENT AUDIT EXHIBIT MG-1: OPERATING EXPERIENCE, RATE BASE AND RATE OF RETURN

Shown in this exhibit are Lockhart's operating experience, rate base, and rate of return for the test year ended December 31, 2005. The exhibit's format is designed to reflect Per Books figures and Proposed Accounting & Pro forma Adjustments, per the Settlement, necessary to normalize the results of Lockhart's test year operations.

As per Column (1), using Total Electric Operations per company's books for the test year ended December 2005, the total income for return of \$1,849,868, and total rate base of \$16,383,954, the computed rate of return was 11.29%. ORS and Lockhart proposed accounting and pro forma adjustments to normalize the operating experience in column (2) calculated as the Total Electric amounts. Column (3), presents after accounting and pro forma adjustments, per settlement, for Total Electric Operations amounts.

The Company's column (4) presents the allocation of the Total Electric booked amount to their Retail Operations. Using Retail Operations, per the Company's filing, total income for return of \$1,373,464, and total rate base of \$12,830,175, the computed rate of return was 10.70%. The proposed accounting and pro forma adjustments, per settlement, were allocated to the Company's Retail Operations in column (5). Column (6) presents Retail Operations amounts after accounting and pro forma adjustments, per settlement, which calculated the total net income for return of

\$1,151,336, total rate base of \$14,387,296, and a resulting rate of return of 8.00%. The Retail Operations proposed increase, per the settlement, of \$919,201 is presented in column (7), along with the related adjustments for taxes and customer growth. Lastly, column (8) presents the after proposed increase per the settlement, which calculates the total income for return of \$1,726,973, rate base of \$14,387,296, and a resulting rate of return of 12.00%.

SETTLEMENT AUDIT EXHIBIT MG-2: EXPLANATION OF ACCOUNTING AND PRO FORMA ADJUSTMENTS

A brief explanation of each accounting and pro forma adjustment on Settlement Audit Exhibit MG-1 is shown in this exhibit. The adjustments were separated between 'Lockhart Total System', 'Settlement Total System', and 'Settlement Retail Operations'. This exhibit shows the proposed accounting and pro forma adjustments made to normalize Lockhart's operations and proposed increase adjustments, per the settlement. For comparative purposes, adjustments agreed to in the settlement and the adjustments proposed by Lockhart in its application are both presented.

SETTLEMENT AUDIT EXHIBIT MG-3: DEPRECIATION AND ACCUMULATED DEPRECIATION ADJUSTMENTS

Per the settlement agreement between the parties, this exhibit shows the computation of the depreciation expense adjustment and accumulated depreciation adjustment based on the pro forma plant in service balances as of September 30, 2006.

SETTLEMENT AUDIT EXHIBIT MG-4: COMPUTATION OF INCOME TAXES

Shown in this exhibit are the computations of state and federal income taxes based on

taxable income after the settlement accounting and pro forma adjustments, and the proposed increase. ORS and Lockhart agreed to use the state income tax rate of 5% and a composite federal income tax rate of 34%.

SETTLEMENT AUDIT EXHIBIT MG-5: COMPUTATION OF CUSTOMER GROWTH

This exhibit shows the computation of customer growth at the rate of .00219 for Lockhart retail customers. After the proposed increase, per settlement, the customer growth adjustment of \$3,783 was calculated based on applying the factor of .00219 to the Net Operating Income of \$1,727,279.

Lockhart Power Company - Docket No. 2007-33-E
Operating Experience, Rate Base, and Rate of Return
For the Test Year Ending December 31, 2005
Docket No. 2007-33-E

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
	Total Electric			Retail Operations				
	Per Books	Proposed Accounting & Pro forma Adjustments Per Settlement	After Accounting & Pro forma Adjustments Per Settlement	Per Books	Proposed Accounting & Pro forma Adjustments Per Settlement	After Accounting & Pro forma Adjustments Per Settlement	Proposed Increase Per Settlement	After Proposed Increase Per Settlement
Operating Revenue								
Rate Revenue	\$20,087,928	(725,088) (1)	19,362,840	13,350,263	(434,910) (1)	12,915,353	919,201 (17)	\$ 13,834,554
Other Revenue	35,442	0	35,442	34,659	0	34,659	0	34,659
Total Operating Revenues	20,123,370	(725,088)	19,398,282	13,384,922	(434,910)	12,950,012	919,201	13,869,213
Operating Expenses								
Purchased Power	12,599,179	(730,332) (2)	11,868,847	7,526,483	(431,932) (2)	7,094,551	0	7,094,551
Production	650,164	210,773 (3)	860,937	387,801	125,895 (3)	513,696	0	513,696
Transmission	169,495	4,851 (4a)	174,346	99,989	2,862 (4a)	102,851	0	102,851
Distribution	555,447	13,904 (4b)	569,351	547,134	13,696 (4b)	560,830	0	560,830
Customer Accounting	314,382	8,618 (4c)	323,000	304,338	8,343 (4c)	312,681	0	312,681
Administrative & General	1,038,089	40,085 (5)	1,078,174	845,444	32,917 (5)	878,361	0	878,361
Regulatory Expense	21,505	6,978 (6)	28,483	16,505	6,978 (6)	23,483	0	23,483
Depreciation	959,529	137,404 (7)	1,096,933	800,542	93,858 (7)	894,400	0	894,400
Amort. FERC License Exp.	24,767	0 (14a)	24,767	14,773	3 (14a)	14,776	0	14,776
Other Taxes	861,722	81,849 (8)	943,571	666,634	59,510 (8)	726,144	3,125 (18)	729,269
State Income Taxes	146,455	0 (9)	146,455	108,764	(16,826) (9)	91,938	45,804 (19)	137,742
Federal Income Taxes	946,096	0 (10)	946,096	702,615	(108,697) (10)	593,918	295,893 (20)	889,811
Amort. Investment Tax Credit	(13,366)	0 (14b)	(13,366)	(10,643)	126 (14b)	(10,517)	0	(10,517)
Total Operating Expenses	\$ 18,273,464	(225,870)	18,047,594	12,010,379	(213,267)	11,797,112	344,822	\$ 12,141,934

Lockhart Power Company - Docket No. 2007-33-E
Operating Experience, Rate Base, and Rate of Return
Test Year Ending December 31, 2005
Docket No. 2007-33-E

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
	Total Electric			Retail Operations				
	Per Books	Proposed Accounting & Pro forma Adjustments Per Settlement	After Accounting & Pro forma Adjustments Per Settlement	Per Books	Proposed Accounting & Pro forma Adjustments Per Settlement	After Accounting & Pro forma Adjustments Per Settlement	Proposed Increase Per Settlement	After Proposed Increase Per Settlement
Income for Return								
Net Operating Income	\$ 1,849,906	\$ (499,218)	1,350,688	\$ 1,374,543	\$ (221,643)	\$ 1,152,900	\$ 574,379	\$ 1,727,279
Plus: Customer Growth	4,051	0 (11)	4,051	3,010	(485) (11)	2,525	1,258 (21)	3,783
Less: Interest on Cust. Dep.	4,089	0	4,089	4,089	0	4,089	0	4,089
Total Income for Return	<u>\$ 1,849,868</u>	<u>(499,218)</u>	<u>1,350,650</u>	<u>1,373,464</u>	<u>(222,128)</u>	<u>1,151,336</u>	<u>575,637</u>	<u>\$ 1,726,973</u>
Original Cost Rate Base								
Plant in Service	35,419,669	3,086,301 (12)	38,505,970	28,203,370	2,066,568 (12)	30,269,938	0	30,269,938
Accumulated Depreciation	16,839,368	788,539 (15)	17,627,907	13,541,463	636,210 (15)	14,177,673	0	14,177,673
Total Net Plant	<u>18,580,301</u>	<u>2,297,762</u>	<u>20,878,063</u>	<u>14,661,907</u>	<u>1,430,358</u>	<u>16,092,265</u>	<u>0</u>	<u>16,092,265</u>
Additions:								
Constr. Work in Progress	561,281	(983) (13)	560,298	412,113	101,992 (13)	514,105	0	514,105
Materials & Supplies	285,734	(4,109) (16)	281,625	201,132	(2,892) (16)	198,240	0	198,240
Cash Working Capital	0	0	0	0	0	0	0	0
Deductions:								
Accum. Def. Income Taxes	2,937,044	0 (14c)	2,937,044	2,338,659	(27,663) (14c)	2,310,996	0	2,310,996
Customer Deposits	106,318	0	106,318	106,318	0	106,318	0	106,318
Total Rate Base	<u>\$ 16,383,954</u>	<u>2,292,670</u>	<u>18,676,624</u>	<u>12,830,175</u>	<u>1,557,121</u>	<u>14,387,296</u>	<u>0</u>	<u>\$ 14,387,296</u>
Rate of Return	<u>11.29%</u>			<u>10.70%</u>		<u>8.00%</u>		<u>12.00%</u>

Lockhart Power Company - Docket No. 2007-33-E
Explanation of Accounting and Pro Forma Adjustments
For the Test Year Ended December 31, 2005
Docket No. 2007-33-E

Description	Lockhart Total System	Settlement Total System	Settlement Retail Operations
<u>Settlement Accounting and Pro forma Adjustments</u>			
(1) Rate Revenue			
A To adjust Purchased Power Agreement (PPA) cost increase due to demand payments to Pacolet Qualified Facility (QF).	38,004	38,004	
B To adjust PPA cost decrease due to Pacolet hydro acquisition.	(138,020)	(138,020)	
C To adjust PPA cost decrease due to new diesel generation.	(630,316)	(630,316)	
D To adjust PPA cost not recovered from lighting rates.	5,244	5,244	
Total	<u>(725,088)</u>	<u>(725,088)</u>	<u>(434,910)</u>
(2) Purchased Power Expense			
A To adjust power cost increase due to demand payments to Pacolet QF.	38,004	38,004	
B To adjust power cost decrease due to Pacolet hydro acquisition.	(138,020)	(138,020)	
C To adjust power cost decrease due to new diesel generation.	(630,316)	(630,316)	
Total	<u>(730,332)</u>	<u>(730,332)</u>	<u>(431,932)</u>
(3) Production Expense			
A To adjust for Pacolet Hydro operating expense.	51,931	51,931	
B To adjust for diesel peaking generator operating expense.	130,057	130,057	
C To adjust for production portion of wages for hourly employees.	30,887	28,785	
Total	<u>212,875</u>	<u>210,773</u>	<u>125,895</u>

Lockhart Power Company - Docket No. 2007-33-E
Explanation of Accounting and Pro Forma Adjustments
For the Test Year Ended December 31, 2005
Docket No. 2007-33-E

Description	Lockhart Total System	Settlement Total System	Settlement Retail Operations
(4) Wage Increase Annualization:			
(4a) Transmission Expense			
A To adjust for the transmission expense portion of wages for hourly and salaried employees.	5,209	4,851	2,862
(4b) Distribution Expense			
A To adjust for the distribution expense portion of wages for hourly and salaried employees.	14,922	13,904	13,696
(4c) Customer Accounting Expense			
A To adjust for the customer accounting expense portion of wages for hourly and salaried employees.	9,238	8,618	8,343
(5) Administrative and General Expense			
A To adjust for administrative expense portion of wages.	27,813	18,897	
B To amortize management transition expenses of \$86,055 over a 3-year period.	28,685	28,685	
C To amortize Pacolet acquisition legal costs of \$31,185 over a 3-year period.	5,000	10,395	
D To adjust for the expense portion of fringe benefits related to wage adjustments.	7,382	2,131	
E To adjust for expenses such as advertising, membership dues, and employee welfare.	0	(20,023)	
Total	68,880	40,085	32,917
(6) Regulatory Expense			
A To amortize rate case expenses of \$70,450 over a 3-year period.	19,600	23,483	
B To remove over amortized prior rate case expenses booked in the test year.	(16,505)	(16,505)	
Total	3,095	6,978	6,978

Lockhart Power Company - Docket No. 2007-33-E
Explanation of Accounting and Pro Forma Adjustments
For the Test Year Ended December 31, 2005
Docket No. 2007-33-E

Description	Lockhart Total System	Settlement Total System	Settlement Retail Operations
(7) Depreciation Expense			
A To adjust depreciation expense to the updated plant balance.	129,365	137,404	93,858
(8) Other Taxes			
A To annualize property taxes for updated plant balances.	75,565	79,190	
B To adjust for the payroll tax expense portion of the wage adjustment.	6,836	5,126	
C To adjust revenue taxes for reduction in revenue.	(2,467)	(2,467)	
Total	79,934	81,849	59,510
(9) State Income Taxes			
A To adjust state income taxes for changes in taxable income due to pro forma adjustments.	(25,914)	0	(16,826)
(10) Federal Income Taxes			
A To adjust federal income taxes for changes in taxable income due to pro forma adjustments.	(167,402)	0	(108,697)
(11) Customer Growth			
A To adjust customer growth for change in Net Operating Income.	(712)	0	(485)
(12) Plant in Service			
A To adjust electric plant for the Pacolet Hydro Acquisition.	350,000	350,000	
B To adjust for the diesel peaking plant addition updated to actual amounts.	1,624,081	1,767,632	
C To adjust for normal additions through September 30, 2006.	968,669	968,669	
Total	2,942,750	3,086,301	2,066,568

Lockhart Power Company - Docket No. 2007-33-E
Explanation of Accounting and Pro Forma Adjustments
For the Test Year Ended December 31, 2005
Docket No. 2007-33-E

Description	Lockhart Total System	Settlement Total System	Settlement Retail Operations
(13) Construction Work in Progress			
A To adjust CWIP to reflect balances as of September 30, 2006.	105,446	105,446	
B To adjust CWIP to remove diesel plant amount included in the plant pro forma adjustment.	(124,297)	(124,297)	
C To capitalize the portion of the wage adjustment applied to CWIP.	12,127	17,868	
Total	<u>(6,724)</u>	<u>(983)</u>	<u>101,992</u>
(14a) Amortization FERC License Expense			
A To amortize FERC License expenses.	<u>0</u>	<u>0</u>	<u>3</u>
(14b) Amortization Investment Tax Credits			
A To amortize investment tax credits.	<u>0</u>	<u>0</u>	<u>126</u>
(14c) Accumulated Deferred Income Taxes			
A To adjust accumulated deferred income taxes.	<u>0</u>	<u>0</u>	<u>(27,663)</u>
(15) Accumulated Depreciation			
A To adjust accumulated depreciation.	<u>780,501</u>	<u>788,539</u>	<u>636,210</u>
(16) Materials and Supplies			
A To adjust materials and supplies balance to reflect a 13-month average balance.	<u>0</u>	<u>(4,109)</u>	<u>(2,892)</u>

Lockhart Power Company - Docket No. 2007-33-E
Explanation of Accounting and Pro Forma Adjustments
For the Test Year Ended December 31, 2005
Docket No. 2007-33-E

Description	Lockhart Total System	Settlement Total System	Settlement Retail Operations
<u>Proposed Increase Per Settlement</u>			
(17) Rate Revenue			
A To adjust for the proposed increase per settlement.			919,201
(18) Other Taxes			
A To adjust gross receipts taxes for the proposed increase per settlement.			3,125
(19) State Income Taxes			
A To adjust for the effects of the proposed increase per settlement.			45,804
(20) Federal Income Taxes			
A To adjust for the effects of the proposed increase per settlement.			295,893
(21) Customer Growth			
A To adjust for the effects of the proposed increase per settlement.			1,258

Lockhart Power Company
Depreciation And Accumulated Depreciation Adjustments
For Test Year Ended December 31, 2005
Docket No. 2007-33-E

Total Electric

(A)	(B)	(C)	(D)	(E)	(F)	(G)	(H)	(I)	(J)	(K)	(L)	(M)
Acct. #	Description	Settlement Pro forma Plant Balance	Depreciation Rates	(C) x (D) Settlement Pro forma Depreciation	Depreciation as of 12/31/05	(E) - (F) Settlement Pro forma Depreciation Adjustments	Settlement Pro forma Amortization	Accumulated Depreciation as of 9/30/06	Settlement Pro forma Depreciation Adjustments	(I) + (J) Settlement Pro forma Accumulated Depreciation	Accumulated Depreciation as of 12/31/05	(K) - (L) Settlement Pro forma Accumulated Depreciation Adjustments
301.000	Organization Expense	403	0.00%				0	0	0	0	0	0
302.000	Franchise & Consents	990,667	2.50%				24,767	152,223	0	152,223	133,650	18,573
	Intangible	991,070					24,767	152,223	0	152,223	133,650	18,573
330.000	Land and Land Rights	314,705	0.00%	0	0	0		0	0	0	0	0
331.000	Structures and Improvements	233,574	2.00%	4,671	4,077	594		151,784	594	152,378	148,726	3,652
332.000	Reservoirs and Dams	3,767,368	1.57%	59,148	57,451	1,697		2,135,274	1,697	2,136,971	2,092,408	44,563
333.000	Waterwheels and Turbines	6,086,580	2.20%	133,905	130,646	3,259		2,132,309	3,259	2,135,568	2,034,360	101,208
334.000	Accessory Electric Equipment	691,369	3.77%	26,065	25,110	955		262,005	955	262,960	243,173	19,787
335.000	Misc. Power Plant Equipment	55,858	2.97%	1,659	1,657	2		31,030	2	31,032	29,787	1,245
336.000	Roads and Railroads	68,205	2.50%	1,705	1,705	0		10,202	0	10,202	8,923	1,279
	Hydro Production	11,217,859		227,153	220,646	6,507		4,722,604	6,507	4,729,111	4,557,377	171,734
340.000	Land & Land Rights	0		0	0	0		0	0	0	0	0
341.000	Structures & Improvements	48,896	5.00%	2,445	0	2,445		0	2,445	2,445	0	2,445
342.000	Fuel Holders, Producers & Acces.	35,562	5.00%	1,778	0	1,778		0	1,778	1,778	0	1,778
344.000	Generator Diesel Peaking	1,589,820	5.00%	79,491	0	79,491		0	79,491	79,491	0	79,491
345.000	Accessory Electric Equipment	0	5.00%	0	0	0		0	0	0	0	0
	Other Production	1,674,278		83,714	0	83,714		0	83,714	83,714	0	83,714
350.000	Land & Land Rights	51,657	0.00%	0	0	0		0	0	0	0	0
352.000	Structures and Improvements	227,105	2.75%	6,245	5,263	982		118,828	982	119,810	119,868	(58)
353.000	Station Equipment	2,217,383	2.75%	60,978	51,624	9,354		1,239,266	9,354	1,248,620	1,230,382	18,238
355.000	Poles and Fixtures	686,968	3.16%	21,708	19,424	2,284		486,029	2,284	488,313	485,322	12,991
356.000	Overhead Cond. and Devices	859,163	2.20%	18,902	18,207	695		488,131	695	488,826	476,832	11,994
	Transmission	4,042,276		107,833	94,518	13,315		2,342,254	13,315	2,355,569	2,312,404	43,165
360.000	Land & Land Rights	25,511	0.00%	0	0	0		0	0	0	0	0
361.000	Structures and Improvements	266,758	2.88%	7,683	7,671	12		121,850	12	121,862	116,098	5,764
362.000	Station Equipment	3,041,886	3.42%	83,652	83,430	222		1,581,193	222	1,581,415	1,545,336	36,079
364.000	Poles, Towers and Fixtures	4,936,698	3.25%	168,835	159,051	9,784		2,018,570	9,784	2,028,354	1,920,096	108,258
365.000	Overhead Cond. And Devices	3,073,764	3.25%	99,897	95,515	4,382		1,934,212	4,382	1,938,594	1,862,435	76,159
367.000	Underground Cond. And Devices	129,720	3.00%	3,892	3,502	390		79,764	390	80,154	76,968	3,186
368.000	Line Transformers	2,672,488	2.76%	73,761	72,659	1,102		1,422,964	1,102	1,424,066	1,371,530	52,536
369.000	Service - Distribution	1,758,481	4.83%	84,935	78,819	6,116		1,120,761	6,116	1,126,877	1,057,655	69,222
370.000	Meters - Distribution	1,477,179	2.97%	43,872	39,319	4,553		362,447	4,553	367,000	381,523	(14,523)
373.000	Street Lighting - Distribution	1,294,101	3.50%	45,294	42,765	2,529		625,661	2,529	628,190	597,005	31,185
	Distribution	18,676,586		611,821	582,731	29,090		9,267,422	29,090	9,296,512	8,928,646	367,866
390.000	Structure and Improvements	389,159	1.62%	6,304	6,298	6		197,182	6	197,188	192,458	4,730
391.000	Office Furniture and Equipment	440,257	10.00%	44,026	43,829	197		287,897	197	288,094	257,903	30,191
392.000	Transportation Equipment	837,801	9.50%	79,591	75,367	4,224		382,596	4,224	386,820	333,656	63,164
394.000	Tools, Shop and Garage	160,831	4.00%	6,433	6,064	369		92,522	369	92,891	92,383	508
395.000	Laboratory Equipment	12,315	5.56%	684	684	(20)		11,650	(20)	11,630	11,137	493
397.000	Communication Equipment	63,738	7.47%	4,761	4,759	2		30,432	2	30,434	26,863	3,571
	General	1,904,101		141,779	137,001	4,778		1,012,279	4,778	1,017,057	914,400	102,657
108.500	Cost of Removal/Salvage							(6,279)	0	(6,279)	(7,109)	830
	Grand Total	36,505,970		1,172,300	1,034,896	137,404	24,767	17,480,503	137,404	17,627,907	16,839,366	788,539
				*Less:	* 75,367							
					1,096,933							
					959,529							

Settlement Depreciation Adjustment

137,404

** Depreciation expense for Laboratory Equipment, which would have normally been computed as \$684, differs from annualized depreciation because the unrecovered balance of this account is \$684.
* Transportation Equipment per books Depreciation is charged to a clearing account and then spread to other functional expenses and capital work based on miles driven on each job.

Settlement Accum. Dep. Adjustment

788,539

Lockhart Power Company
Computation of Income Taxes
For the Test Year Ended December 31, 2005
Docket No. 2007-33-E

	After Accounting & Pro Forma Adjustments Per Settlement	After Proposed Increase Per Settlement
Total Operating Revenues	\$ 12,950,012	\$ 13,869,213
Less: Operating Expenses	11,111,256	11,114,381
Less: Annualized Interest Expense	<u>0</u>	<u>0</u>
State Taxable Income	1,838,756	2,754,832
State Income Taxes @ 5%	91,938	137,742
Less: State Taxes Per Books & After Accounting & Pro Forma Adjustments	<u>108,764</u>	<u>91,938</u>
State Income Tax Adjustments	<u>(16,826)</u>	<u>45,804</u>
 Federal Taxable Income (State Taxable Income - State Income Taxes)	 1,746,818	 2,617,090
Federal Income Tax Rate @ 34%	593,918	889,811
Total Federal Income Taxes Per Books & After Accounting & Pro Forma Adjustments	<u>702,615</u>	<u>593,918</u>
Federal Income Tax Adjustments	<u>(108,697)</u>	<u>295,893</u>

Lockhart Power Company
Computation of Customer Growth
For the Test Year Ended December 31, 2005
Docket No. 2007-33-E

	Retail Per Books	Proposed Accounting & Pro forma Adjustments Per Settlement	After Accounting & Pro forma Adjustments Per Settlement	Proposed Increase Per Settlement	After Proposed Increase Per Settlement
Net Operating Income	1,374,543	(221,643)	1,152,900	574,379	1,727,279
Growth Factor	0.00219	0.00219	0.00219	0.00219	0.00219
Customer Growth Adjustment	\$ 3,010	\$ (485)	\$ 2,525	\$ 1,258	\$ 3,783

THE OFFICE OF REGULATORY STAFF
SETTLEMENT TESTIMONY AND EXHIBITS
OF
A. RANDY WATTS



MAY 18, 2007
DOCKET NO. 2007-33-E

APPLICATION OF LOCKHART POWER
COMPANY, FOR GENERAL INCREASE IN
ELECTRIC RATES

SETTLEMENT TESTIMONY OF A. RANDY WATTS

FOR

THE OFFICE OF REGULATORY STAFF

DOCKET NO. 2007-33-E

**IN RE: APPLICATION OF LOCKHART POWER COMPANY FOR A RATE
INCREASE**

**Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS AND
OCCUPATION.**

A. My name is Randy Watts. My business address is 1441 Main Street, Suite 300, Columbia, South Carolina 29201. I am employed by the State of South Carolina as Program Manager in the Electric Department for the Office of Regulatory Staff ("ORS").

**Q. PLEASE STATE YOUR EDUCATIONAL BACKGROUND AND
EXPERIENCE.**

A. I received a Bachelor of Science Degree in Electrical Engineering from the University of South Carolina in Columbia in 1976. I was employed at that time by the Public Service Commission of South Carolina ("Commission") as a Utilities Engineer in the Electric Department and was promoted to Chief of the Electric Department in August 1981. Subsequent to internal Commission restructuring, my position was redesignated Chief of Electric in October 1999. I remained in that role until transferring to my current position with ORS in January 2005. I have testified on numerous occasions before the Commission in

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Post Office Box 11263 (29211)
Columbia, SC 29201**

1 conjunction with fuel clause, complaint, territorial assignment, Siting Act and
2 general rate proceedings.

3 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS**
4 **PROCEEDING?**

5 **A.** The purpose of my testimony is to provide a summary of the Electric
6 Department's examination of Lockhart Power Company's ("the Company" or
7 "Lockhart") Application for a general increase in its electric rates under Docket
8 No. 2007-33-E. In addition I will provide an overview and support for the
9 Settlement Agreement reached by the parties in this proceeding.

10 **Q. MR. WATTS, WHAT AREAS WERE COVERED BY THE ELECTRIC**
11 **DEPARTMENT IN THIS PROCEEDING?**

12 **A.** The Electric Department was responsible for reviewing and analyzing the
13 Company's proposal pertaining to the inclusion of additional generating facilities,
14 Cost of Service Studies, rate design, revenue distribution, depreciation rates, and
15 certain Pro Forma adjustments.

16 **Q. PLEASE PROVIDE THE RESULTS OF ORS'S ANALYSIS OF THE**
17 **COMPANYS PROPOSED INCLUSION OF ADDITIONAL GENERATING**
18 **FACILITIES IN ITS FLEET.**

19 **A.** The additional generating units are composed of two distinct projects. One
20 is comprised of three 1,825 kW diesel peaking generators while the second is the
21 purchase of an 800 kW hydroelectric generating facility previously contracted to
22 provide its output to Lockhart under the Qualifying Facility ("QF") requirements
23 of the Public Utility Regulatory Policies Act of 1978 ("PURPA"). With the

1 corresponding reduction in Purchase Power expenses as a direct consequence of
2 these projects, there results a net economic benefit to the retail ratepayers. The
3 Company should be commended for its insight and diligence particularly with
4 respect to the acquisition and installation of the peaking units.

5 **Q. PLEASE DESCRIBE THE COST OF SERVICE STUDIES PERFORMED**
6 **BY THE COMPANY.**

7 **A.** The Company performed four cost of service studies for this case
8 including Historical, Pro Forma, Equal Rates of Return and Proposed. The
9 Historical is based on actual test year per book data; the Pro Forma results from
10 adjustments to the per book data; the Equal Rates of Return comes from inclusion
11 of the Pro Forma adjustments along with setting class revenues in order to yield
12 equal returns for each class of customer; and lastly the Proposed Study
13 incorporates the Pro Forma adjustments and the proposed revenues by class which
14 the Company is requesting in this proceeding. The methodology used to perform
15 these studies is identical to those presented in prior cases and approved by the
16 Commission. These Studies allocate the demand related production and
17 transmission costs on the twelve month coincident peak ("12 CP") method.
18 Lockhart obtains the majority of its power from Duke Energy under a wholesale
19 purchase agreement. Duke Energy's demand billing component for Lockhart is
20 based on Lockhart's actual monthly coincident demand at the time of Duke
21 Energy's monthly peak load. This billing methodology justifies the use of the
22 monthly CP as the appropriate allocation method for Lockhart's demand related
23 costs. These Studies separate the Company's revenues, expenses, and rate base

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1 items between jurisdictions and among classes in order to determine each one's
2 contribution to its cost of service. ORS has reviewed these Studies and found
3 them to be reasonably developed and appropriate for use in this proceeding.

4 **Q. PLEASE EXPLAIN THE RATE DESIGN UTILIZED BY THE COMPANY**
5 **IN ITS PROPOSED TARIFFS.**

6 **A.** The basic rate designs of the proposed tariffs remain unchanged from the
7 previously approved structure, although various modifications were incorporated
8 in some rate components. These were made to reflect the class revenue
9 requirements and cost allocations as determined by the Proposed, Pro Forma Cost
10 of Service Study. In Addition, the level of Purchased Power in the base rates is
11 proposed to be reduced to reflect a decrease in these costs associated with the
12 operations of the previously discussed additional generating facilities included in
13 the Company's fleet.

14 **Q. PLEASE EXPLAIN HOW THE REVENUE REQUIREMENTS WERE**
15 **DETERMINED FOR EACH CUSTOMER CLASS.**

16 **A.** The Pro Forma Cost of Service Study was utilized to determine the proper
17 cost allocation for each class, then revenues were applied to bring the class returns
18 more in line with the overall return requested. This is an appropriate and equitable
19 method of allocating revenue requirements and is accepted regulatory practice.

20 **Q. DID ORS REVIEW THE DEPRECIATION RATES UTILIZED BY THE**
21 **COMPANY IN THIS CASE?**

22 **A.** Yes. We confirmed that the Company used the depreciation rates
23 previously approved by the Commission to determine the appropriate cost levels

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1 for depreciation expense in its current filing. Since the Company did not
2 previously have any diesel generators in its production fleet, it therefore did not
3 have an established depreciation rate for this category. The Company utilized a
4 depreciation rate of 5.0% based on a twenty (20) year life expectancy for these
5 peaking diesel generators. ORS believes this life expectancy to be reasonable and
6 appropriate for these assets. Research by ORS enabled us to receive substantiation
7 from another utility operating similar peaking facilities within the State that the
8 expected normal lifetime of its comparably operated units is twenty (20) years.
9 As with all depreciation rates, they are subject to modification from time to time
10 as actual experience impacts the data upon which these rate levels are set.

11 **Q. PLEASE EXPLAIN THE REMAINING PRO FORMA ADJUSTMENT**
12 **NOT PREVIOUSLY COVERED FOR WHICH THE ELECTRIC AREA IS**
13 **RESPONSIBLE.**

14 **A.** Customer growth was calculated using the standard regulatory approach
15 historically used and accepted by this Commission for many years. In this case the
16 customer growth factor was determined by taking the year ending number of
17 Lockhart's retail customers and dividing it by the average for the test period,
18 minus one (1), to obtain the appropriate factor to apply to the retail net operating
19 income after adjustments. ORS concurs with the Company's calculation of the
20 customer growth 'factor' of 0.00219; however using ORS's retail net operating
21 income after the increase of \$574,379 as shown on Audit Exhibit MG-1 page 2 of
22 2, results in a customer growth of \$1258.

1 **Q. MR. WATTS, WOULD YOU PLEASE PROVIDE AN OVERVIEW OF**
2 **THE SETTLEMENT AGREEMENT REACHED BY THE PARTIES IN**
3 **THIS PROCEEDING?**

4 **A.** All parties in this proceeding have worked together and reached a
5 comprehensive settlement of all issues pending in this case. The parties are of the
6 opinion that this settlement agreement will result in rates which are adequate, just,
7 reasonable, non-discriminatory, and supported by the evidence of the record of
8 this proceeding, and will allow the Company the opportunity to earn a reasonable
9 rate of return. Based upon negotiations an agreement was reached that will reduce
10 the proposed net increase from \$592,722 to \$484,291 or approximately 18.29%.
11 The Company proposed net increase of \$592,722 results from reducing the
12 proposed base rate revenue increase of \$1,027,632 by the reduction in Purchased
13 Power Adjustment revenue of \$434,910 created by the additional generating
14 facilities. This amount of \$434,910 is shown in Company Application Exhibit A3-
15 1, line 1, column 4, as well as Settlement Audit Exhibit MG-1, page 1 of 2,
16 column 5. Netting this same Purchased Power Adjustment revenue reduction of
17 \$434,910 against the Settlement base rate revenue increase amount of \$919,201
18 shown on Settlement Audit Exhibit MG-1, page 1 of 2, column 7, results in the
19 agreed upon net revenue increase amount of \$484,291.

20 **Q. PLEASE EXPLAIN HOW THE REDUCTION IN THE COMPANY'S**
21 **REQUEST WAS APPLIED.**

22 **A.** This reduction in Lockhart's requested increase was applied to the
23 Residential and Industrial classes of customers only. The objective was to modify

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1 the Industrial Rate Schedule I charges such that no customer's billing resulted in
2 an increase relative to the current rate. Once that was accomplished the remaining
3 revenues would be used to determine the appropriate reductions to be applied to
4 the energy component of the Residential tariffs. The results of these modifications
5 are shown on my Settlement Exhibit ARW-1. There is one (1) Industrial Service
6 tariff (Schedule I) and two (2) Residential Service tariffs (Schedules R and RA)
7 that were affected by these rates changes. These three (3) tariffs are provided as
8 Settlement Exhibits ARW-2, ARW-3, and ARW-4 respectively. No changes were
9 made to any of the other Company proposed tariffs. The Parties are in agreement
10 that the Settlement Revenue Increase along with the corresponding revenue
11 distribution to the classes and the resulting tariff charges are fair, just and
12 reasonable and provide the Company an opportunity to recover the revenue
13 required to earn a fair return on its investment. ORS supports the Settlement
14 Agreement and requests it be approved and adopted by the Commission.

15 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

16 **A.** Yes, it does.

**SOUTH CAROLINA
OFFICE OF REGULATORY STAFF**

**APPLICATION OF LOCKHART POWER COMPANY
FOR GENERAL INCREASE IN ELECTRIC RATES**

DOCKET NO. 2007-33-E

A. RANDY WATTS SETTLEMENT TESTIMONY

SETTLEMENT EXHIBIT INDEX

<u>EXHIBIT NO.</u>	<u>EXHIBIT TYPE</u>
ARW-1	Proposed Revenue Increase and Settlement Revenue Increase Comparison
ARW-2	Lockhart Power Company: Rate Schedule I - Industrial Service
ARW-3	Lockhart Power Company: Rate Schedule R - Residential Service
ARW-4	Lockhart Power Company: Rate Schedule RA - Residential Service (All Electric)

All Exhibits Prepared by the SC Office of Regulatory Staff

**Office of Regulatory Staff
Proposed Revenue Increase and
Settlement Revenue Increase Comparison
for Lockhart Power Company**

Docket No. 2007-33-E

Customer Class	Company Proposed Revenue Increase	Settlement Revenue Increase	% Reduction	Settlement Rate of Return
Residential	\$541,265	\$476,164	-	11.14%
Commercial	\$4,699	\$4,699	-	12.50%
Industrial	\$0	(\$43,330)	-	13.90%
Street Lighting	\$5,203	\$5,203	-	11.64%
Outdoor Lighting	\$41,555	\$41,555	-	11.58%
Total Retail	\$592,722	\$484,291	-18.29%	12.00%

LOCKHART POWER COMPANY
SCHEDULE I
INDUSTRIAL SERVICE

AVAILABILITY

Available only to establishments classified as "Manufacturing Industries" by the Standard Industrial Classification Manual, 1957 or later revision, published by The Bureau of Budget, United States Government, and only where 85% or more of the total energy consumption of such establishment is used for its manufacturing processes.

Service under this Schedule shall be available only to customers with a metered demand of 500 kilowatts or more served from the Company's transmission system, or customers served under this Schedule prior to the effective date of this Schedule.

Service under this Schedule shall be used solely by the contracting Customer in a single enterprise, located entirely on a single, contiguous premises.

This Schedule is not available for auxiliary, breakdown or standby service; and power delivered hereunder shall not be used for resale or exchange or in parallel with other electric power, or as a substitute for power contracted for or which may be contracted for, under any other schedule of the Power Company, except at the option of the Company, under special terms and conditions expressed in writing in the contract with the Customer.

The obligations of the Company in regard to supplying power are dependent upon its securing and retaining all necessary rights-of-ways, privileges, franchises and permits, for the delivery of such power, and the Company shall not be liable to any Customer or Applicant for power in the event it is delayed in, or is prevented from furnishing the power by its failure to secure and retain such rights-of-ways, rights, privileges, franchises and permits.

TYPE OF SERVICE

The Company will furnish 60 cycle service through one meter, at one delivery point, at one of the following approximate voltages, where available:

Single phase, 120/240 volts; or

3 phase, 208Y/120 volts, 460Y/265 volts; or

3 phase, 3 wire, 240, 460, 575, or 2300 volts; or

3 phase, 4160Y/2400, 12470Y/7200 volts; or

3 phase voltages other than the foregoing, but only at the Company's option, and provided that the size of the Customer's contract warrants a substation solely to serve that Customer, and further provided that the Customer furnish suitable outdoor space on the premises to accommodate a ground-type transformer installation, or substation, or a transformer vault built in accordance with the Company's specifications.

The type of service supplied will depend upon the voltage available. Prospective Customers should ascertain the available voltage by inquiry at the office of the Company before purchasing equipment.

Motors of less than 5 h.p. may be single-phase. All motors of more than 5 h.p. must be equipped with starting compensators and all motors of more than 25 h.p. must be of the slip ring type except that the Company reserves the right, when in its opinion the installation would not be detrimental to the service of the Company, to permit other types of motors.

(Schedule I continued)

LOCKHART POWER COMPANY
SCHEDULE I
INDUSTRIAL SERVICE

(Schedule I continued)

MONTHLY RATE

Demand Charge:
\$2.60 per kW of Billing Demand

Energy Charge:
For the First 200 Hours Use of Billing Demand per Month:
6.00 cents per kWh for the first 50,000 kWh
4.66 cents per kWh for all additional kWh.
For all kWh in excess of 200 hours use of Billing Demand:
3.51 cents per kWh.

Plus Purchased Power Adjustment Clause

DETERMINATION OF BILLING DEMAND

The demand for billing purposes each month shall be the maximum integrated thirty-minute demand in the current month, but not less than 75 percent of the contract demand, nor less than 200 kilowatts.

Where more than one meter is used to meter a single customer located entirely on a single contiguous premises, the demand meters will be arithmetically added to determine the monthly demand.

MINIMUM BILL

The monthly minimum bill shall be \$3.80 per kW of Billing Demand.

POWER FACTOR CORRECTION

When the average monthly power factor of the Customer's power requirements is less than 85 percent, the Company will correct the integrated demand in kilowatts for that month by multiplying by 85 percent and dividing by the average power factor in percent for that month.

PAYMENT

Bills under this Schedule are due and payable at the office of the Company on or before the tenth day after the date of the bill.

CONTRACT PERIOD

Each Customer shall enter into a contract to purchase electricity from the Company for a minimum original term of one (1) year; but the Company may require a contract for a longer original term of years where the requirement is justified by the circumstances. Either party may terminate the contract at the end of the original term by giving at least sixty (60) days' previous notice of such termination in writing.

LOCKHART POWER COMPANY
SCHEDULE R
RESIDENTIAL SERVICE

AVAILABILITY

Available only to residential customers in residences, condominiums, Mobile homes, or individually-metered apartments for lighting, cooking, water heating, heating, refrigeration and incidental use.

TYPE OF SERVICE

The Company will furnish 60 cycle service through one meter, at one delivery point, at one of the following approximate voltages where available:

Single phase, 120/240 volts, or

3 phase, 208Y/120 volts, or other available voltages at the Company's option.

Motors in excess of 2 h.p. frequently started, or arranged for automatic control, must be of a type to take the minimum starting current and must be equipped with controlling devices approved by the Company.

Three phase service will be supplied, if available. Where three phase and single phase service is supplied through the same meter it will be billed on the rate below. Where the three phase service is supplied through a separate meter it will be billed on the applicable General Service Schedule.

RATE

Customer Charge \$6.50 Per Month

Plus: 8.22 Cents Per kWh for the first 1,000 kWh used per month

9.24 Cents Per kWh for all over 1,000 kWh used per month

Plus Purchased Power Adjustment Clause

EXCESS CAPACITY CHARGE

Demand meters may be installed by the Company on any installation served under this Schedule. When the measured hourly demand in any month exceeds 10 kW, a charge of \$1.00 will be made for each whole kW in excess of 10, which charge will be in addition to the charge for the kWh used.

PAYMENT

Bills under this schedule are due and payable at the office of the Company on or before the due date shown on the bill.

CONTRACT PERIOD

The original term of this contract shall be one year and thereafter until terminated by either party on thirty days written notice.

LOCKHART POWER COMPANY
SCHEDULE RA
RESIDENTIAL SERVICE, ALL-ELECTRIC

AVAILABILITY

Available only to residences, condominiums, Mobile Homes, or individually-metered apartments in which the energy required for all water heating, cooking and environmental space conditioning is supplied electrically.

Service under this Schedule shall be used solely by the individual customer in a single residence, condominium, Mobile Home, single apartment and all electric energy used in such dwelling must be recorded through a single meter.

To qualify for service under this Schedule, the environmental space conditioning system and a separate electric water heater must be permanently installed in accordance with sound engineering practices and the manufacturer's recommendations.

TYPE OF SERVICE

The Company will furnish 60 cycle service through one meter, at one delivery point, at one of the following approximate voltages, where available:

Single phase, 120/240 volts; or
3 phase, 208Y/120 volts, or other available voltages at the Company's option.

Motors in excess of 2 h.p. frequently started, or arranged for automatic control, must be a type to take the minimum starting current and must be equipped with controlling devices approved by the Company.

RATE

Customer Charge \$6.50 per month
Plus: 8.22 cents per kWh for the first 1,000 kWh used per month
 *9.24 cents per kWh all over 1,000 kWh used per month
 Plus Purchased Power Adjustment Clause

*During the months of October, November, December, January, February, March and April this rate will be 6.46 cents.

PAYMENT

Bills under this Schedule are due and payable at the office of the Company on or before the due date shown on the bill.

CONTRACT PERIOD

The original term of this contract shall be one year and thereafter until terminated by either party on thirty days written notice.